MONTHLY UPDATE
MAY 2022

21 YEARS
Protecting India with Pride

HDFC Life
Sar utha ke jiyo!

May, 2022

"Chains of habit are too light to be felt until they are too heavy to be broken."

\- *Warren Buffet*

Equity markets

Indices	31st May 2022	29th Apr 2022	1 Month Return (%)	1 Year Return (%)
BSE Sensex	55,566	57,061	-3%	7%
S&P CNX Nifty	16,585	17,103	-3%	7%
BSE 100	16,888	17,575	-4%	7%
BSE Mid Cap	23,144	24,418	-5%	6%
BSE Small Cap	26,371	28,612	-8%	12%

Source: Bloomberg

During May'22, domestic equity indices had a subdued performance - large cap indices fell 3-4% MoM while the mid and small cap index underperformed, down 5% and 8% MoM, respectively. On a 1-year basis, the Small cap index has outperformed the large and mid cap indices. Over the past one year, Sensex and Nifty were up ~7% each while BSE Mid cap and Small cap index were up 6% and 12% respectively.

During May'22, performance across the sector indices was mixed. The performance ranged from -16% to +5%. Auto and FMCG sector gained the most; up 5% and 1% respectively while Metals and Consumer Durables sector underperformed; down 16% and 11% respectively. On a 1-year basis, Utilities sector is the best performing sector gaining 50% followed by Realty and Capital Goods sector respectively. Healthcare and Metals are the bottom two sectors; down 8% and 4% each respectively.

The yield of benchmark 10-year G-sec moved to 7.42% at the end of May'22 from 7.14% at the end of Apr'22.

Global equity indices were mostly flat during the month. The NASDAQ and CAC40 were the worst performing indices, down 2% and 1% respectively during the month. On a 1 year basis, FTSE 100 has gained the most, up 8%.

Commodities (USD)	1 Month Return (%)	One Year Return (%)
Gold	-3%	-23%
Silver	-5%	-29%
Crude Oil	12%	77%
Copper	-2%	-8%
Aluminum	-9%	12%
Lead	-4%	0%
Nickel	-11%	57%
Tin	-14%	7%
Zinc	-5%	29%

Source: Bloomberg

All major commodities fell during May'22 except Crude which rose 12% MoM. Tin and Nickel fell the most, down 14% and 11% respectively.

On a YoY basis, most major commodities have posted YoY gains. Nickel has appreciated the most up 57% YoY.

Macro Economic Data

Indicators	Feb-22	Mar-22	Apr-22	May-22	Comments
IIP (YoY, %)	1.5%	1.9%			Industrial output marginally grew by 1.9% yoy in Mar’22 vs. 1.5% yoy growth in Feb’22, mainly led by the increase in electricity output (6.1% yoyin Mar'22) . On the other hand Manufacturing output marginally grew by 0.9% yoy in Mar'22.
Core Sector (YoY, %)	6.0%	4.9%	8.4%		Core sector output grew by 8.4% yoy in Apr’22 led by the increase in coal output (28.8%) and Refinery Products (9.2%).
RBI monetary policy (Repo Rate) (%)	4.00	4.00	4.00	4.9 (Jun'22)	RBI increased the repo rate in June to 4.9% following a 40bps increse in a off-cycle meeting in May'22.
CPI inflation (%)	6.1%	7.0%	7.8%		CPI inflation rose to 7.8% in Apr’22 from 7% in Mar’22, led by the increase in food inflation from 8.1% in Apr’22 to 7.5% in Mar’22
Trade Deficit ($, bn)	-20.9	-18.5	-20.1	-23.3	In May’22, exports grew by 15.5% to $37.3bn, while imports grew by 56.1% to $60.6bn, as a result trade deficit widened to $23.3bn in May’22 vs. $20.1bn in Apr’22.
GST Collection ($, bn)	1330	1421	1675	1409	Total gross GST revenue collections in May’22 stood at Rs. 1,409bn, following Rs. 1,675bn collection in Mar’22.
FII Flows-Equity ($, bn)	-4.74	-5.38	-2.24	-5.18	On equity side, FPIs sold $5.18bn in May’22, following an outflow of $2.24bn in Apr’22. On debt side, FII sold $0.72bn in May’22, following an outflow of $0.58bn in Apr’22.
FII Flows-Debt ($, bn)	-0.41	-0.74	-0.58	-0.72	
Exchange Rate (INR/USD)	75.49	75.81	76.42	77.60	Indian Rupee depreciated by 1.5% during Apr'22, as it closed at 77.6 in the end of May’22 from 76.4 at the end of Apr’22 per dollar.
GDP (%)					Real GDP grew by 4.1% in Q4 FY22 vs. 5.4% in Q3 FY22 and 8.5% growth in Q2 FY22. The lower GDP growth was led by lower HH consumption (1.8%) while fixed investment grew 5.1%. GDP grew 8.7% in FY22, following 6.6% contraction in FY21.

Outlook

India was a relative underperformer in May when compared to both developed and emerging markets, with MSCI World and MSCI Emerging markets ending flat for the month. However, MSCI India has outperformed both World and Emerging Market on Calendar YTD basis. Global markets continue to battle key concerns of global economic slowdown amid aggressive policy tightening, Russia-Ukraine conflict and continued lockdowns in China. US Federal Reserve raised its benchmark interest rate by 50 bps and minutes of May FOMC meeting signaled 50 bps rate hikes in next meetings.

Global uncertainties continue to weigh on FII flows to India. FIIs remained net sellers of Indian equities in May with selling of $4.7bn. This marked the 8th consecutive month of net equity outflows for FIIs, with YTD outflows of $22.1bn. DIIs recorded inflows of $6.6bn in May, maintaining the buying trend observed since March 2021. Monetary easing in FY19-20 helped drive down real yields and re-rate equities and now monetary tightening in 2022 is driving up real yields and de-rating equities. The risk remains India’s significant P/E premium to World and EM.

On the economy front in India, May CPI inflation surged to an 8-year high of 7.79% and WPI inflation jumped to 15.1% in May. March IIP growth remained lackluster at 1.9%. 4QFY22 real GDP growth slowed to 4.1% from 5.4% in 3QFY22. RBI in a surprise move hiked policy rates by 40bps and CRR by 50 bps after having kept rates unchanged in the April MPC meet where it had raised inflation forecasts and lowered growth outlook. The Govt. of India also announced a range of measures to curb rising prices – cutting excise duty on petrol and diesel, imposing export duties on steel products and reducing import duties on coal and naphtha.

In Q4FY22 BSE100 Sales and EBIT rose 24% and 19% respectively. Headline operating margins fell 150 bps YOY ex-banks, suggesting inflation helped the top-line, but not the bottom-line. Corporate result season does hint at challenges for corporate profitability in FY23 due to slowing global and domestic growth, elevated commodity prices, rising interest rates and uneven economic recovery. However, India’s diversified earnings profile should act as a cushion against any steep downgrades. Indian markets long term earnings outlook continues to be robust and recent market correction is leading to valuation regressing towards its long term average of 17X FY24e. We believe investors should do well to navigate the near term with patience as we remain optimistic from a medium to long term point of view as we expect a cyclical recovery in the economy and earnings after several years of sub-par growth.

Fixed Income Market

Fixed Income Market Review

With inflationary pressures visible among all major developed and emerging markets, expectations of rate hikes by the Central Bankers have kept bond yields elevated. In a surprise move the MPC increased the Repo rate by 40bps to 4.40% after a long pause of almost 2 years. The shorter end of the yield curve was the worst hit resulting in the curve flattening. The MPC also hiked CRR by 50bps to suck out excess liquidity from the system, the hike effectively removed INR 90,000crs from the system. The move was largely driven by expectations of inflation moving up further. Brent Crude Oil prices continued to remain elevated as the Russia-Ukraine war carries on. Brent crude oil closed higher at USD 123 per barrel higher from the last month close of USD 107 per barrel. Inflation in US continued to remain elevated with inflation remaining above 8%. The US 10yr yield rose sharply to 3.19% during the month before cooling down to 2.84 for the month of May 22. Government has also taken fiscal measures to fight inflation. Excise duty on petrol and diesel were brought down by INR 8/litre and INR 6/litre respectively while the LPG subsidy was reduced for beneficiaries of Ujjawala Scheme. This excise cut will likely result in a fiscal strain of INR 1 trn as per government estimates. Further, the government also announced additional fertilizer subsidy of INR 1100 bn and LPG subsidy of INR 61 bn. Apart from LPG and fertilizer, the government had increased food subsidy for 6-months under free-food programme. The government also successfully divested its stake in LIC raking in INR 210 bn from its IPO. Although it is still early in the year, the fear of additional borrowing kept yields high. The domestic 10yr benchmark bond closed at 7.42% against 7.14% at the end of the previous month. Among data releases, India’s April CPI rises to eight year high of 7.79% vs March CPI of 6.95%. Core inflation (CPI Ex-Food Ex-Fuel) too shot to its 8 year high of 7% from its previous reading of 6.3%. Headline WPI inflation for March 2022 rose sharply to 15.1%, compared to 14.5% recorded in March 2022. This is the highest year on year reading in the series so far.

FY22 GDP growth printed at 8.7%, a little lower than the 2nd revised estimate of 8.9%. India’s Q4 FY22 GDP grew by 4.1% YoY while GVA grew 3.9% YoY. India’s trade deficit in March came at $18.5 bn lower than USD 20.9 bn of February. Among other economic data, IIP growth for March 2022 came at 1.85%, marginally higher than the reading of 1.46% in February 2022. Goods and Services Tax (GST) revenue collection for May came at Rs 1,40,885 cr. India's Nikkei Markit Manufacturing PMI remained flat to 54.6 in May 2022, against 54.7 in the previous month, and the Services PMI rose sharply to 57.9 in April from 53.6 in the previous month. Composite PMI rose to 57.6 in April 22 vs 54.3 in the previous month.

Market Outlook –

With inflation surprising on the upside across all major economies, central bankers have started raising interest rates or are in the process of raising it. With the ongoing war between Russia and Ukraine getting prolonged with no end visible, commodity prices remain elevated stoking fear of persistent high inflation across the globe. Post the out of the turn policy hike of 40bps reinforcing its commitment to fight the rising inflation, the MPC is likely to front load the rate hikes to curb the rising inflation. This coupled with a steady and heavy supply of bonds is expected to keep the yields elevated. Emerging markets are also likely to face pressure with regard to inflation and a depreciating currency as foreign capital rushes to safe haven assets.

Although the government is working towards easing inflation by cutting excise duty and increasing the fertilizer subsidy, the fiscal strain on the other hand can prove detrimental for the bond markets. Although it's too early in the year to revise the fiscal numbers, as we progress toward the second half of the year, the fiscal math will get clearer. Soaring commodity prices, coupled with monetary policy normalization, a large bond supply and an adverse global bond yields environment are expected to lead to further hardening of bond yields, though any measures taken by RBI to provide support to the bond markets may slow down the pace of yield movements.